

Energy and Technology Committee Michigan House of Representatives

Prepared slides of
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Outline

- Costs of regulation versus restructuring
- Residential prices
- Virginia and re-regulation
- Policy considerations

Determining the Costs and Benefits of Regulation and Restructuring

■ Added costs of regulation*

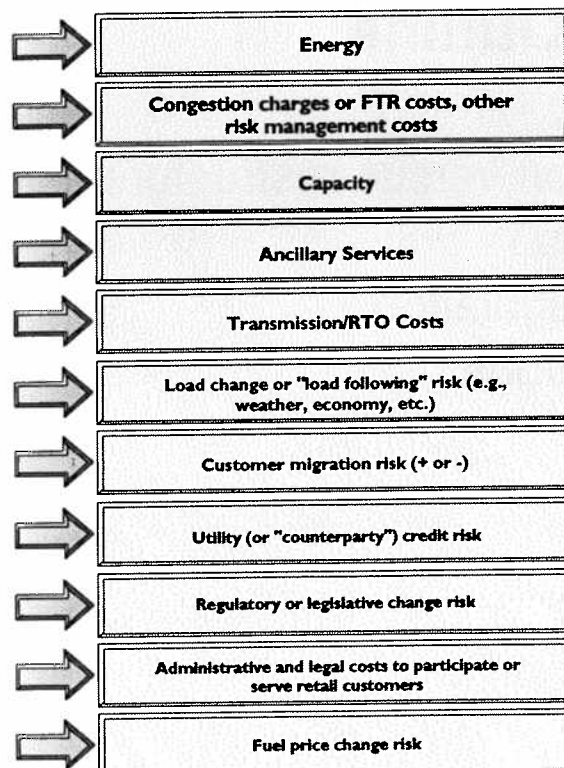
- ▶ over capitalization
- ▶ operation cost inefficiencies
- ▶ regulatory compliance cost
- ▶ resource allocation inefficiencies

■ Added costs of restructuring*

- ▶ market power efficiency loss
- ▶ de-integration costs, from loss of vertical economies
- ▶ ISO/RTO formation and operation costs
- ▶ ISO/RTO complexity
- ▶ increased cost-of-capital required for investment
- ▶ under investment in electric supply infrastructure

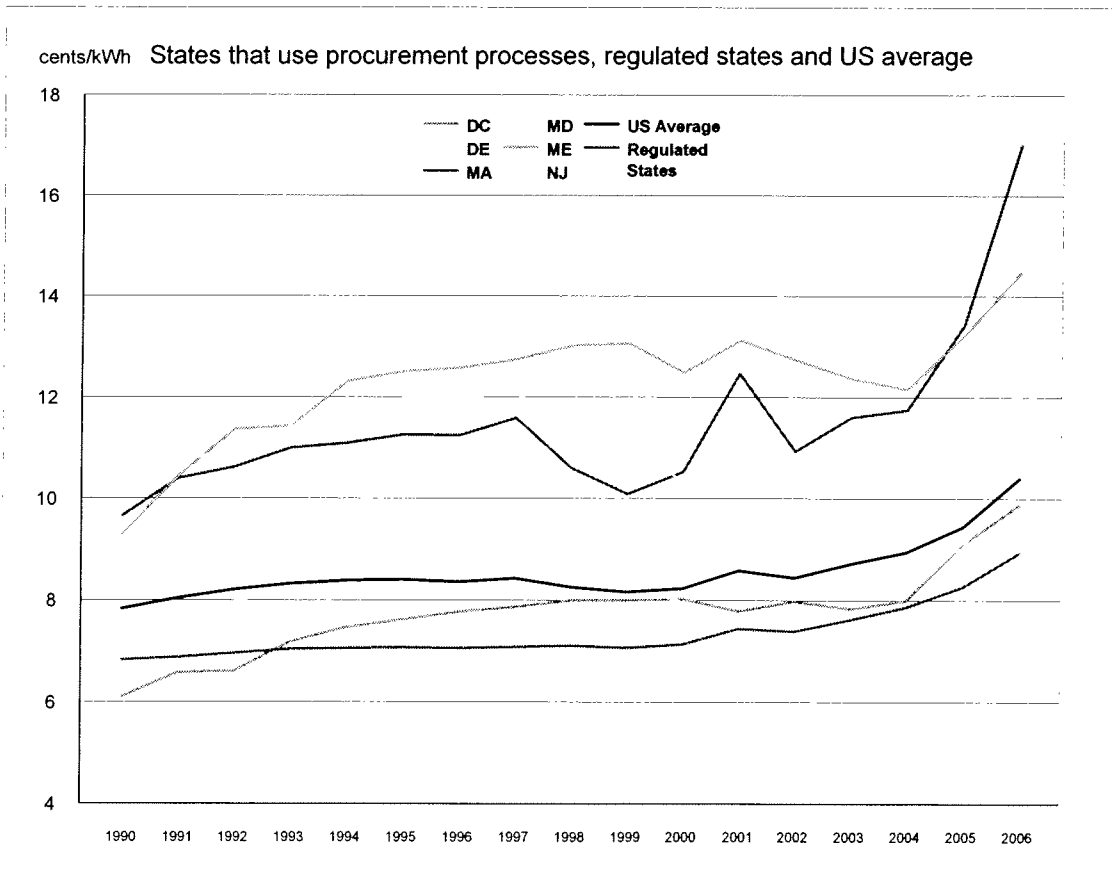
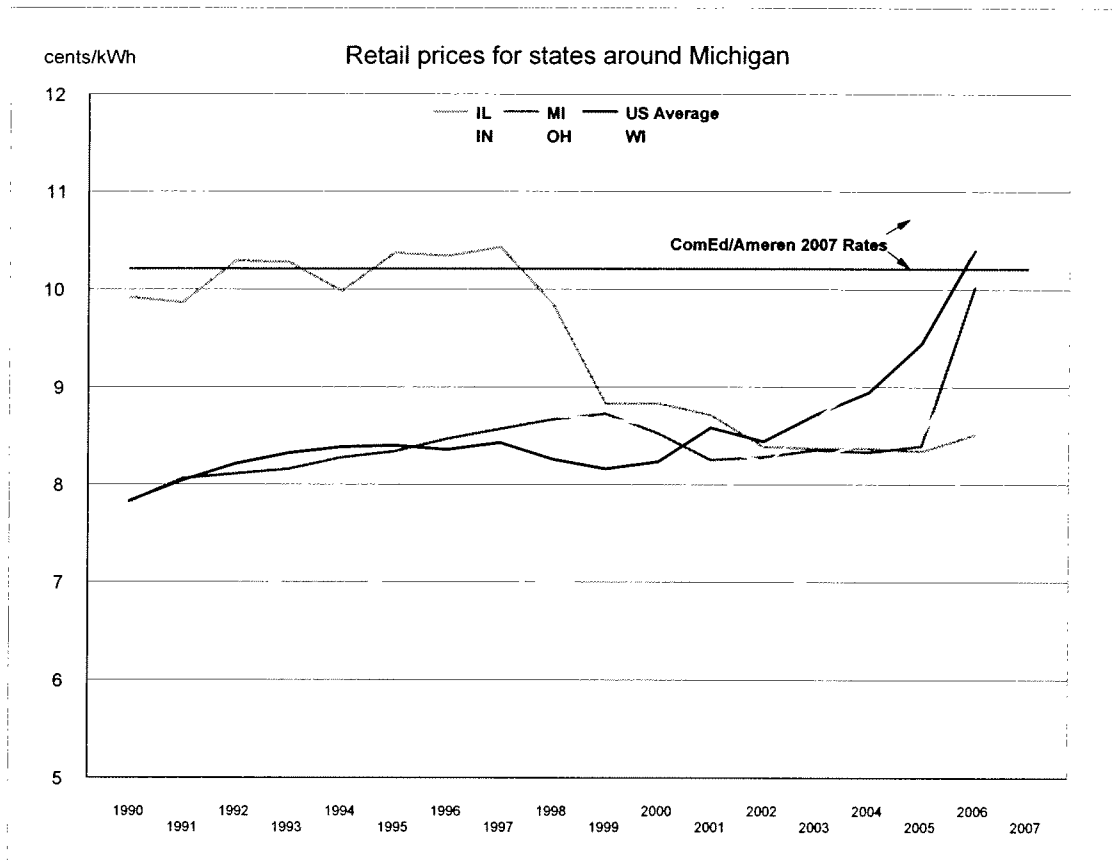
*Added to the cost of supply in a perfectly competitive market.

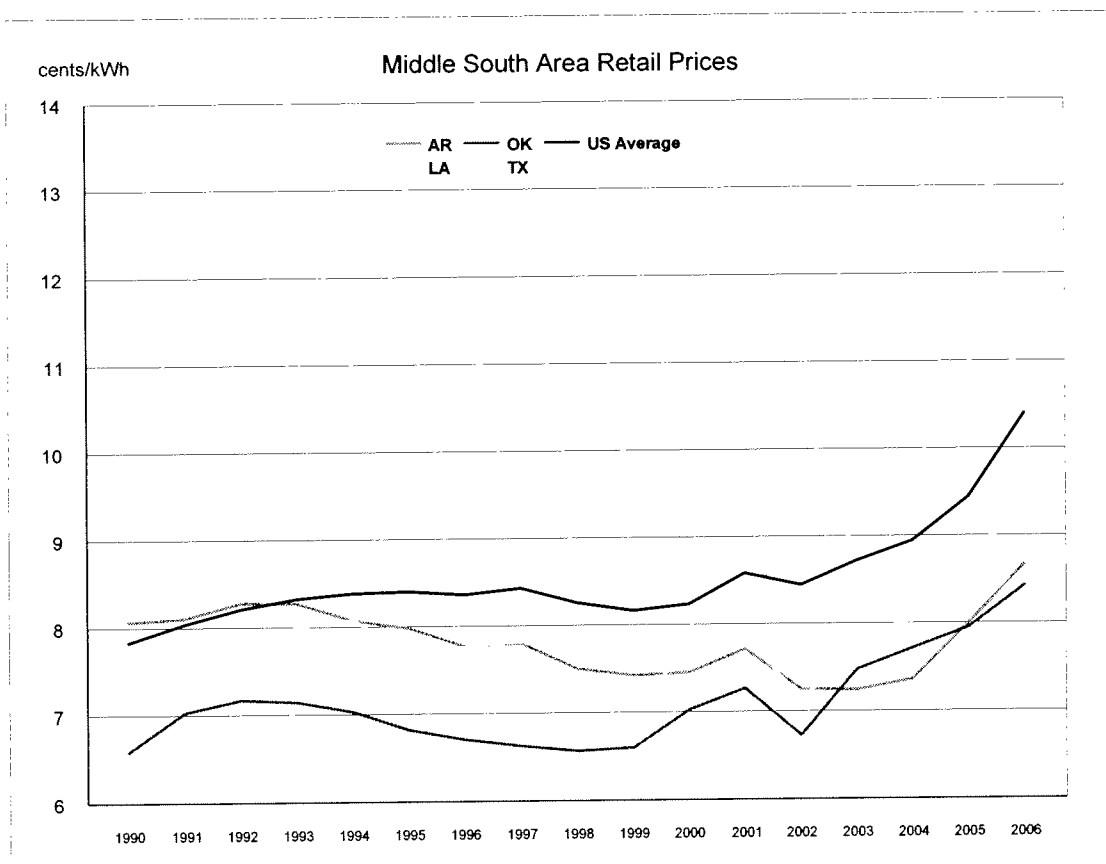
Costs of "full requirements" service to retail customers*



- ✓ The sum of the parts may be greater than the whole (due to loss of vertical economies and new costs and risks)
- ✓ Experience in other states shows that if this sum is greater than the retail price, there's no shopping or offers from suppliers
- ✓ If this sum is less than the retail price, there are offers and shopping
- ✓ The catch is -- to get the latter result, the price will likely exceed the regulated price
- ✓ Some of these costs did not exist with regulation

*Not all costs may apply in all cases.





Recent Virginia Re-Regulation Legislation

- End of rate cap period moved from up Dec. 31, 2010 to Dec. 31, 2008
- Ends retail access for most customers (except those >5 MW -- with conditions for return)
- State Corporation Commission (SCC) determines fair rate of return on common equity (ROR)
 - cannot be lower than the average ROR of a "peer group" in the southeastern US.
 - cannot be higher than 300 basis points above that average
 - ROR increases capped by CPI
 - ROR may increase or decrease by a Performance Incentive up to 100 basis points
 - 1/2 of one percent dead-band region, with (asymmetrical) true-up
- Rate adjustment clauses to recover specified costs
- "Enhanced" ROR for specified generation technologies
- SCC required to consider petitions for rate adjustment clauses stand-alone, that is, without regard to other utility costs or revenues
- This is not recommended for Michigan

If you continue with restructuring

- Should the state maintain state jurisdiction of generation resources?
 - will federal regulators have Michigan's best interest in mind?
 - should Michigan PSC be given authority to approve any transfer of generation assets?
 - would any future transfer of generation assets (not happening now) put Michigan in the same spot as those procurement states?
- Don't close out future options
- Don't wait for a crisis to act

If you discontinue restructuring

- Consider the importance of PSC discretion in determining appropriate rate-of-return, cost recovery, etc.
- Consider extending PSC authority to include performance-based or incentive regulations when appropriate
- Consider that there are more than two options, that is, re-regulate using traditional regulation or staying on the present course
 - also suspension of retail access or limiting to larger customers

Final Thoughts

- We have seen several different retail access models: California, Pennsylvania, New Jersey, Maryland, and Texas
 - with similar results
- Will we start to see more impact on reliability?
- How do we stimulate adequate and appropriate levels of investment?
- Markets are a means to an end, not an end in itself